Statement of

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Introduction

Mr. Chairman, thank you for inviting me today to present the Administration's views on H.R. 2944, the Electricity Competition and Reliability Act. DOE, the Agency responsible for formulating and implementing the Clinton Administration's energy policies, is a strong proponent of comprehensive Federal electricity restructuring legislation. On April 15, Secretary Richardson transmitted to Congress the Comprehensive Electricity Competition Act (CECA)[1] – the Administration's vision for the role the Federal government should play in the transition to competition.

At the same time FERC continues to promote competition in the wholesale markets, 24 states have now adopted electricity restructuring proposals that allow for competition at the retail level. Almost every other state has the matter under active consideration. The Clinton Administration believes that this is a positive development. Competition, if structured properly, will be good for consumers, good for the economy and good for the environment. Companies that had no incentive to offer lower prices, better service, or new products will now compete for customers. Consumers will save money on their electric bills. Lower electric rates will also make businesses more competitive by lowering their costs of production. By promoting energy conservation and the use of cleaner and more efficient technologies, greenhouse gas emissions will be reduced, as will emissions of conventional air pollutants. However, the full benefits promised by competition can be realized only within an appropriate Federal statutory framework.

[1]The Administration transmitted CECA to Congress in two separate parts. The first part, which was introduced by Congressman Bliley and Dingell (upon request) as H.R. 1828 on May 17, includes all of the non tax-related provisions in the Administration's proposal. Both parts were introduced in the Senate by Senators Murkowski and Bingaman (upon request) – S. 1047 and S. 1048 – on May 13.

What we do at the Federal level, and when we do it, will have a profound impact on the success of state and local retail competition programs.

Mr. Chairman, I want to commend you and the other members of this Subcommittee for the effort you are putting forth in an attempt to enact comprehensive electricity restructuring legislation. Many of the issues are complex and controversial. Nevertheless, it is vitally important to consumers, the economy and the environment that these issues be resolved in an appropriate manner.

I also want to thank you for the courtesy which you and your staff have shown to me, Secretary Richardson and other members of the Clinton Administration. I believe that working together, in a bipartisan fashion, the Administration and members on both sides of the aisle can achieve a result that will benefit all Americans.

Let me begin with three points:

- It is critical that Congress pass comprehensive electricity restructuring legislation sooner, rather than later.
- Restructuring legislation can succeed only if it is developed on a bipartisan basis. And
- Although the bill includes some encouraging provisions, the Administration does not support H.R. 2944 in its current form. We would like to work with you to achieve a version of restructuring legislation that we could all support.

Federal Action is Critical

While some state competition programs are already in effect, tens of millions of additional consumers will soon have the ability to choose their power in those states

implementing retail competition programs over the next 2-3 years. As the states continue to move forward, the absence of action at the Federal level is creating significant uncertainty in the increasingly regionalized power and transmission markets. The fact is, if we don't act at the Federal level, the benefits from state restructuring programs will be limited.

- First, competition is not going to work if transmission lines operate under different sets of rules and requirements. It is essential that all wholesale and retail power marketers have non-discriminatory access to the wires that transport their product. While the Federal Energy Regulatory Commission (FERC) has jurisdiction over the transmission of electricity in interstate commerce, FERC's authority is somewhat limited. Congress needs to ensure that all major transmission facilities are, to the extent practicable, subject to comparable FERC open access requirements.
- Second, independent regional transmission organizations (RTOs) will help promote efficient, competitive and reliable markets. However, FERC's authority over, and ability to require, RTO formation remains uncertain. Congress must address these uncertainties.
- Third, as we move to a more competitive environment, the reliability of our bulk power systems can no longer be entrusted to voluntary standards. Significant support has developed for a proposal to have an electric reliability organization, overseen by FERC, establish mandatory reliability standards. Congress should authorize the development and enforcement of mandatory reliability standards.
- Fourth, restructuring efforts won't succeed if competitive markets are not developed. While open transmission access and the formation of independent regional transmission organizations should go a long way towards changing the monopoly structure of the

electric utility industry to competition, the fact is that some utilities may have horizontal market power as a result of their control over a substantial amount of generating capacity, enabling them to crowd-out potential competitors and keep the price of power artificially high. Congress must empower FERC to prevent incumbent utilities from using market power to inhibit competition.

- Fifth, existing programs that provide support for renewable energy and other important public benefits were designed for a system of regulated markets. Congress should act to ensure that these public benefits are not lost as a result of the transition to competition.
- Sixth, certain Federal statutory provisions may impede the efforts of the states and FERC to promote competition. Congress needs to eliminate these impediments and modernize those statutes which are inconsistent with the development of fully competitive markets.
- Seventh, the statutes governing the operation and regulation of Federal utilities – the Tennessee Valley Authority (TVA) and the Federal Power Marketing Administrations (PMAs) – must be revised to allow for effective competition in the regions they serve.

Mr. Chairman, the Federal government clearly has an important role to play in the transition to competition. While the states are moving forward rather briskly, Congress has yet to act. The Federal government needs to send the appropriate signals about what the rules of the road will be in this new world of competition. Instead, we are sending signals of confusion.

The electricity markets are crying out for the certainty that is necessary before essential investments are made. Generating capacity reserve margins have significantly tightened. The construction of new major transmission facilities has dramatically slowed. Aging distribution facilities are beginning to wear out.

Several regions of the country have experienced major problems in recent summers. As the heat and humidity rose, some utilities found it increasingly difficult to meet consumer demands. Spot prices for electricity rose dramatically. Elected officials and utility executives made urgent public appeals for conservation. Factories were forced to shut down their operations and send workers home. Some areas experienced rolling blackouts. Other areas lost power due to failures in overworked and outdated distribution facilities. While it is difficult to attribute all of these problems to the uncertainties surrounding the transition to competition, they clearly have played a significant role. In short, Mr. Chairman, we can't afford to wait until the 107th Congress to do what needs to be done now.

Need for Bipartisan Approach

The electricity sector is our nation's most capital-intensive industry, holding assets with a book value of approximately $700 billion. In addition, electricity affects our everyday lives and businesses. It is not at all a stretch to point out that access to power can sometimes be a matter of life and death. This is a major industry that is in the process of a monumental transition.

Very few major congressional initiatives are accomplished in the absence of a bipartisan approach and with cooperation from both ends of Pennsylvania Avenue. Mr. Chairman, electricity restructuring is not a partisan issue. Members on both sides of the aisle have offered thoughtful and meaningful proposals that merit consideration, including a bipartisan bill introduced earlier this year by Congressmen Largent and Markey. DOE encourages you to continue your efforts to develop a bipartisan bill that will enable Congress to enact comprehensive restructuring legislation that can be supported by the Administration.

Comments on H.R. 2944

Mr. Chairman, we commend you for including a number of positive provisions in H.R. 2944, such as those intended to enhance reliability, protect consumers and promote aggregation. Clearly, your legislation addresses many of the key issues that need to be included in a comprehensive electricity restructuring bill. However, we believe H.R. 2944 should be modified to establish the necessary ground rules and adjustments required for the transition to competition.

I would like to take a few minutes to discuss, in some detail, the Department's views on four important issues: (1) market power; (2) FERC jurisdiction over transmission; (3) regional transmission operators; and (4) public benefits programs. Thereafter, I will briefly comment on H.R. 2944's treatment of several other items.

Market Power

The primary goal of Federal electricity restructuring legislation must be to aid the transition to competition in a manner that allows consumers to benefit through lower rates. However, significant rate savings can't be achieved if effective competition fails to develop.

Open transmission access and the creation of independent regional transmission organizations should go a long way towards achieving competitive markets. However, access to transmission is, by itself, not enough. Utilities that own substantial amounts of generation in a region or strategically located facilities may be able to raise prices above competitive levels and inhibit the entry of new competitors through horizontal market power. Because electricity markets are becoming increasingly regional and multi-regional, state regulators cannot adequately address market power issues. As a result, it is essential that the Federal government, as the guardian of interstate commerce, be able to take aggressive action during the transition

period to ensure that utilities are unable to use horizontal market power to control prices and impede competition.

The antitrust laws are not, by themselves, sufficient to address the market power problems a newly-restructured electricity industry may face. The traditional regime of rate-of-return regulation has led to high concentrations of ownership of generation facilities regulation. As the Department of Justice recently noted in testimony before this Subcommittee:

> The antitrust laws do not outlaw the mere possession of monopoly power that is the result of skill, accident, or a previous regulatory regime. Antitrust remedies are thus not well-suited to address problems of market power in the electric power industry that result from existing high levels of concentration in generation or vertical integration."

FERC currently has the authority to condition merger applications to remedy potential market power. Absent a merger application, FERC's only other available tool to address market power is to deny a request for market-based rates. However, denying such requests could severely impede the Commission's ability to promote wholesale competition.

To ensure that the development of competition is not hindered by the exercise of market power, the Administration's legislation would authorize FERC to remedy concentrations of market power in the wholesale market, including the authority to order the divestiture of assets, if market power is found. In addition, our bill would enable FERC to provide backup market power remedies for the retail market, at the request of a state. This is important because some states seeking to open their markets to retail competition may not have clear statutory authority to remedy market power problems in their state or have jurisdiction over facilities in other states that may be the cause of a market power problem.

Mr. Chairman, we are disappointed that H.R. 2944 fails to address horizontal market power. We recommend that the bill be modified to incorporate the market power provisions in

the Administration's bill.

Jurisdiction over Transmission

FERC Orders No. 888 and 889 have had a tremendous positive impact in promoting wholesale competition by requiring jurisdictional utilities to provide competitors access to transmission facilities under rates and terms comparable to those provided to itself. Unfortunately, FERC's open access authority does not directly extend to non-jurisdictional utilities, such as most cooperative and municipal utilities, as well as TVA and the PMAs. The Department supports the provisions in H.R. 2944 which extend FERC's regulatory authority to the transmission facilities owned by previously non-jurisdictional utilities.

We are concerned, however, about FERC's ability to prevent discriminatory transmission access as a result of a recent 8th Circuit Court of Appeals decision -- Northern States Power v. FERC. In that case, the Court essentially ruled that FERC has no authority to prevent a utility from denying access to others in favor of its own bundled retail sales.

H.R. 2944 states that FERC would have authority only over the unbundled transmission of electricity that is sold at retail, while state regulators would have jurisdiction over transmission when it is part of a bundled retail sale. It is necessary that all transmission owners and all transmission services be subject to similar rules and requirements. The distinction in H.R. 2944, in light of the 8th Circuit decision, would balkanize the regulation of transmission and could have a potentially chaotic impact on the development of competitive markets. FERC would be unable to prevent a utility providing transmission services that are bundled with the retail sale and distribution of power from discriminating against other electricity suppliers in favor of its own generation. State regulators, which would have jurisdiction over bundled transmission services,

may not have sufficient incentives to adequately police a utility's use of its transmission lines, especially if the competing supplier were seeking access to sell power to consumers located in another state.

Mr. Chairman, we urge you to reevaluate this provision. Whether transmission is bundled or unbundled, it is essential to the development of competitive markets that all competitors have non-discriminatory access to the facilities.

Regional Transmission Organizations

Properly sized, independent, regional transmission organizations (RTOs) can provide significant benefits, including the enhancement of reliability and the promotion of more efficient and competitive markets. FERC's recent Notice of Proposed Rulemaking, which encourages transmission-owning utilities to participate in RTOs, is a positive step. However, this voluntary approach does not ensure that appropriate RTOs will be developed.

The Department is encouraged that H.R.2944 would require all transmitting utilities to join RTOs and we generally support the standards for RTO formation laid out in the bill – (1) independence, (2) appropriate scope and regional configuration, (3) operational control over all transmission facilities comprising the RTO, (4) responsibility for planning transmission additions and upgrades, and (5) other standards FERC determines are in the public interest.

We are concerned that the legislation limits FERC's discretion in approving an RTO. While an RTO might meet the standards set out in the legislation, it might very well not be the optimal RTO for a particular region. However, H.R. 2944 would prohibit FERC from disapproving a less-than-optimal proposal as long as the proposed RTO met the statutory standards. In addition, FERC's hands would be tied with regard to RTOs approved prior to the

date of enactment. Although a previously approved RTO might require alteration due to changes in circumstances, FERC would be powerless to alter it. In addition, this provision could have a chilling effect on FERC's grants of approvals for new RTOs prior to the date of enactment, if FERC knows that it could not require changes to an RTO following the date of enactment of the legislation.

Moreover, although we support the concept of incentive pricing policies in certain limited situations, it is unclear why FERC should be required to establish a pricing policy designed to encourage transmitting utilities to form RTOs (and extend the policies to already existing RTOs), when the legislation already requires transmitting utilities to join RTOs. It is important to remember that transmission will continue to be a monopoly function. Any deviation from cost-of-service ratemaking should be limited to exceptional circumstances.

Public Benefits

While retail competition has the potential to increase renewable energy's share of the electricity market, the inherent uncertainty of the transition to competition, the recognition of important environmental and energy diversification benefits from renewables, and the fact that existing Public Utility Regulatory Policies Act requirements are incompatible with competition and ineffective under present market conditions suggest that Federal policy towards renewable electricity should be revisited in the context of restructuring.

Mr. Chairman, DOE commends you for recognizing the need to address renewable energy in restructuring legislation. We support the extension of both the Renewable Energy Production Incentive (REPI) program for municipal and cooperative utilities and the wind and biomass tax credits. However, more needs to be done; otherwise, the progress we have made in renewables

could be partially lost during the transition to competition because these technologies have not yet achieved cost-competitiveness. The inclusion of a renewable portfolio standard would provide market-based support for the development and deployment of renewable energy technologies. Unlike the mandatory purchase provisions of PURPA, this approach would be consistent with competitive electricity markets.

In addition, we continue to be concerned that retail competition could lead to reduced support for programs that provide important public benefits. Under cost-of-service regulation, programs supporting and promoting research and development, energy efficiency and low-income assistance were supported, in part, through utility rate structures. As utilities prepare for competition, they will be unwilling to include in their rates the cost of programs not included in the rates of their competitors. A public benefits fund, which provides matching funds to the states for low-income assistance, energy efficiency programs, consumer education and the development and demonstration of emerging, clean technologies, should alleviate these concerns.[2]

Other Issues

Mr. Chairman, while I cannot comment on each and every provision in H.R. 2994, I would like to briefly discuss several additional issues.

· **Target Date/Opt-Out –** Mr. Chairman, the Department recognizes that since Chairman Bliley dropped his insistence on Federally-mandated competition, the debate over

[2]The Administration's public benefits fund proposal also includes a rural safety net in the unlikely event that competition adversely impacts rural areas.

restructuring legislation has shifted to other issues. Nevertheless, we continue to believe that there is substantial merit to establishing a target date for the implementation of retail competition and requiring state utility commissions and non-regulated municipal and cooperative utilities to hold proceedings to examine the benefits or costs of adopting retail competition programs. I know we both share the opinion that competition, if it is structured properly, will benefit all classes of consumers. Most, if not all, state utility commissions and non-regulated utilities would likely come to the same conclusion after a thorough examination.

- **Transmission Siting** – We are pleased that H.R. 2944 recognizes that regional solutions to transmission siting issues are both appropriate and necessary. In addition, the Administration has no objections to providing FERC with authority to order transmission-owning utilities to expand their facilities, as long as state siting authority is not diminished.
- **Reliability** – As I discussed earlier, one of the most critical elements of comprehensive electricity restructuring legislation is the need for mandatory reliability standards. The reliability title of H.R. 2944 closely mirrors the language included in the Administration's legislation and language proposed by the North American Electric Reliability Council. We believe the differences between these proposals can be resolved.
- **Consumer Protection –** H.R. 2944 contains several vitally important consumer protection provisions, including items related to information disclosure, consumer privacy and measures designed to prohibit marketers from engaging in slamming and cramming practices. We fully support these provisions.

- **Mergers –** We are pleased that H.R. 2944 retains FERC's authority under Section 203 of the Federal Power Act to review utility mergers and extends FERC's jurisdiction over mergers that involve generation-only and utility holding companies. Utility mergers are not necessarily anti-competitive. However, it is vital that FERC – the regulatory agency with significant experience with and understanding of electricity markets – be able to prohibit or condition a merger that would have a deleterious impact on retail or wholesale competition.[3]

- **Reciprocity –** The Administration believes that each state should have the authority to determine whether to prohibit a utility not fully subject to retail competition requirements from participating as a marketer in that state if the state has implemented retail competition. Recognizing that H.R. 2944 instead imposes a Federal reciprocity requirement, we believe the requirement would be ineffective. By allowing utilities not subject to retail competition to avoid the reciprocity limitation by simply filing an open access plan with a state utility commission, the legislation could very well allow utilities that file sham proposals to escape the intent of the reciprocity provision. We think this provision should be modified.

- **Aggregation –** Mr. Chairman, the Administration commends you for including Section 541 in H.R. 2944. This provision will help entities that are interested in aggregating to

[3] To avoid inadvertent impacts on small consumer-owned systems, the Administration bill excludes entities with existing loans made or guaranteed under the Rural Electrification Act from merger review requirements.

increase consumers' purchasing power and enable them to reap the full benefits of retail competition.

- **Interconnection –** We welcome the inclusion of a Federal interconnection standard in H.R. 2944. Distributed power and combined heat and power technologies can enhance both reliability and the environment. We believe a more expansive approach than that included in the bill is required. Interconnection should not be restricted based on ownership or the ability to serve nearby facilities. In addition, we believe that regulatory and tax barriers that inadvertently discourage the use of these technologies should be addressed.

- **Federal Utilities –** We are pleased to see that the key issues associated with Federal utilities which the Administration believes need to be addressed in restructuring legislation, as well as the general approach to resolving these issues, are included in H.R. 2944. Although Title VI of the legislation differs in certain limited respects from the Administration's proposed restructuring legislation, both bills share the same goal – enabling competition to thrive in the regions served by Federal utilities. We believe the differences between the two approaches can be resolved.

- **Private-Use Prohibition –** We agree that it is necessary to resolve the issues surrounding the tax treatment of debt issued by municipal utilities to enable them to fully participate in competitive markets. The small differences between the provisions in H.R. 2944 and the Administration's proposed legislation should be easily bridged.

Conclusion

Mr. Chairman, while the states are proceeding with their restructuring programs, all eyes

are on Congress to learn what signals the wholesale and retail markets will receive. This Committee's leadership has been essential and will continue to be. Although we do not support H.R. 2944 in its current form, the Administration's approach to comprehensive restructuring legislation has many elements in common with your proposed legislation. And I know that several members of this Subcommittee, on both sides of the aisle, have put forth proposals that merit serious consideration.

We are confident that a bipartisan bill can be reported out of the Subcommittee soon. Secretary Richardson and I, as well as our staff, stand ready to assist you and the other Subcommittee members in this vital endeavor. Only by working together can we take the steps that are necessary to provide consumers with the full benefits of competition.